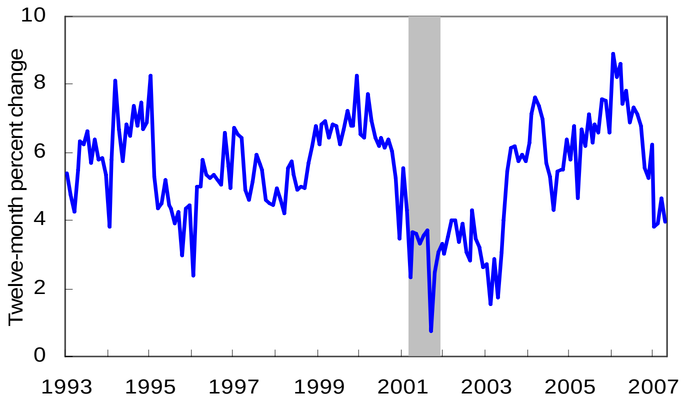
Joint Economic Committee
WEEKLY ECONOMIC DIGEST
Senator Charles Schumer, Chairman
Congresswoman Carolyn Maloney, Vice Chair
May 14, 2007

ECONOMIC NEWS

Retail Sales Slumped in April

Retail sales dropped in April. Sales at retail establishments and food services declined by 0.2 percent last month, after increasing by 1.0 percent in March. Sales of motor vehicles and parts dropped 1.0 percent last month, but that drop was partly offset by a 1.7 percent rise in gasoline sales. Excluding the volatile month-to-month changes in automotive sales, retail sales declined by 0.2 percent in April to a level that is only 4.0 percent higher than a year earlier (see chart).

Retail Sales Excluding Motor Vehicle and Gasoline Sales



Source: Bureau of Labor Statistics, U.S. Department of Labor and National Bureau of Economic Research.

The trade gap widened in March. Both exports and imports of goods and services rose in March, but the rise in imports ($8.2 billion) exceeded the rise in exports ($2.2 billion). As a result, the deficit for international trade in goods and services (imports minus exports) increased by $6.0 billion to $63.9 billion. The March rise in the trade deficit was substantially higher than most analysts had anticipated.

Gasoline prices continued to climb in recent weeks. The retail price of regular grade gasoline averaged $3.05 dollars per gallon last week. That was the highest average price since the hurricanes struck the Gulf Coast in September 2005. Retail gasoline prices have risen by about 90 cents per gallon since the end of January. While the Department of Energy continues to expect prices to moderate somewhat in coming weeks, it has raised its price projection over the past month. The Department now predicts that the retail price of regular grade gasoline will average $2.95 per gallon over the summer season (April through September), or about 11 cents per gallon more than last summer.

IN FOCUS

Focus on the Fed's Decision

Last week, the Federal Reserve decided to hold its target interest rate for overnight federal funds unchanged at 5¼ percent. The language of the Fed's latest announcement was virtually identical to its previous announcement in March. The Fed's latest decision was widely anticipated. But the decision did little to change the dilemma that has faced the Fed for much of the past year: how to respond to a combination of weak growth and elevated trend inflation?

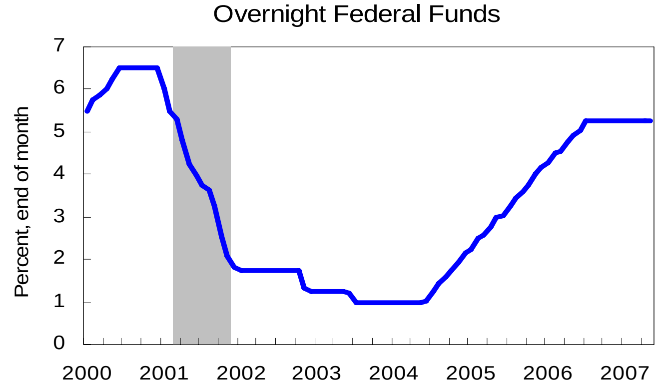
The Fed has a dual mandate to control inflation and to promote sustainable economic growth with high employment. Those goals are believed to be consistent and compatible over the long run, because the economy is most likely to achieve sustainable economic growth with high employment if inflationary expectations remain contained.

When the economy is particularly weak, the risk of inflation is generally small and the Fed can keep interest rates low in order to stimulate demand. The Fed cut its target interest rate sharply in 2001 as the economy weakened and there was a perceived risk that it could weaken even further in the wake of the September 11th terrorist attacks (see Snapshot). The Fed kept its target interest rate very low (1.0 percent) until mid-2004.

Continued on reverse...

SNAPSHOT

Federal Reserve's Target Interest Rate on Overnight Federal Funds



Source: Board of Governors, Federal Reserve System.
The gray area indicates a period of recession as defined by the National Bureau of Economic Research.

THE WEEK AHEAD

DAY	UPCOMING RELEASES
TUESDAY 15	Consumer Price Index (April 2007)
WEDNESDAY 16	New Residential Construction (April 2007) Industrial Production and Capacity Utilization (April 2007)
THURSDAY 17	Weekly Report on Unemployment Insurance Claims (Week ending May 5)
FRIDAY 18	University of Michigan Survey of Consumer Sentiment (May 2007, preliminary)

TUESDAY, MAY 15th: Rising energy prices contributed to April inflation in the Consumer Price Index

ECONOMIC STATS AT A GLANCE

	MONTH			QUARTER			YEAR	
KEY INDICATORS	May	Apr	Mar	2007 Q1	2006 Q4	2006 Q3	2006	2005
Real GDP Growth (%)	—	—	—	1.3	2.5	2.0	3.3	3.2
Unemployment (% of labor force)	4.5	4.4	4.5	4.5	4.5	4.7	4.6	5.1
Labor Productivity Growth (%)	—	—	—	1.7	2.1	-0.5	1.6	2.1
Labor Compensation Growth (%)	—	—	—	3.2	3.6	3.6	3.1	3.3
CPI-U Inflation (%)	n.a.	7.4	4.9	3.8	-2.1	3.1	3.2	3.4
Core CPI-U Inflation (%)	n.a.	1.2	2.4	2.3	1.9	3.0	2.5	2.2

Sources: Bureau of Economic Analysis, U.S. Department of Commerce; Bureau of Labor Statistics, Department of Labor.

Notes: Except where otherwise noted, values in the table represent percent changes at seasonally adjusted annual rates. Productivity is output per hour worked in private non-agricultural establishments. The Employment Cost Index is for civilian workers in government and business. Core CPI-U inflation is the percent change in the CPI-U excluding food and energy as reported by the Bureau of Labor Statistics.

IN FOCUS (Continued)

When the economy is relatively strong and markets tight, there is a danger that the demand for goods and services might consistently exceed supply and the Fed is likely to keep interest rates relatively high to prevent the economy from overheating and inflation from rising. By mid-2004, there was widespread agreement that some tightening of monetary policy (raising interest rates) was appropriate as the economy began to show signs that it might finally be recovering from the 2001 recession and that action from the Fed might prevent the economy from overheating . Beginning in June 2004, the Fed raised its target rate by ¼ percentage point at each of 17 consecutive FOMC meetings until the rate reached 5¼ percent in June 2006. As rates kept rising, however, the focus shifted to a debate over the relative risks of the Fed's tightening too much and choking off the recovery or not tightening enough and allowing inflation to rise too much.

The FOMC has kept its target funds rate at 5¼ percent at its last eight meetings since last June, but the debate continues as to whether weak growth or elevated inflation should be the Fed's main concern. In its decision last week, the Fed retained the anti-inflationary stance it had adopted in March, reiterating that their "predominant policy concern remains the risk that inflation will fail to moderate as expected." But the statement also reiterated that monetary policy decisions are "data driven", meaning that the FOMC will closely monitor incoming data on the economy as it balances the risks that economic growth will be too slow against the risks that inflation will be too high.

Data released through the end of last week suggest that the economy may have grown more slowly in the first quarter than the anemic 1.3 percent annual rate in the Commerce Department's advance estimate. Additionally, April's retail sales and employment reports were disappointing. But the Fed will have a broader picture of recent growth and inflation indicators to examine when it next meets, in late June, to decide monetary policy. For now, financial markets continue to expect that the Fed will not change its target funds rate any time soon.